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SHARLEY & MOORE, ATTORNEYS AT LAW  
SAN FRANCISCO, CALIF.

IN THE  
SUPREME COURT OF THE UNITED STATES

OCTOBER TERM, 1938

No. **745** **15**

L. BOTELEB, Trustee of the Estate of RICH-  
MAID CREAMERIES, INC., a corporation,  
Debtor, *Petitioner,*

vs.

RAY INGELS, Director of Motor Vehicles of  
the State of California; HOWARD E.  
DEEMS, as Registrar of Motor Vehicles of  
the State of California, and the MOTOR  
VEHICLE DEPARTMENT OF THE  
STATE OF CALIFORNIA, *Respondents.*

No. **746** **16**

L. BOTELEB, Trustee of RICHMAID  
CREAMERIES, INC., a corporation, Debtor,  
*Petitioner,*

-vs.

RAY INGELS, Director of Motor Vehicles of  
the State of California, and HOWARD E.  
DEEMS as Registrar of Motor Vehicles of  
the State of California, *Respondents.*

RESPONDENTS' BRIEF

✓ EARL WARREN,

Attorney General of  
the State of California,

✓ By FRANK W. RICHARDS,

Deputy Attorney General of  
the State of California,

*Counsel for Respondents.*



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# In the Supreme Court

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E. BOTELER, Trustee of RICHMAID  
CREAMERIES, INC., a corporation, Debtor,  
vs. *Petitioner,*

RAY INGELS, Director of Motor Vehicles of  
the State of California, and HOWARD E.  
DEEMS as Registrar of Motor Vehicles of  
the State of California, *Respondents.*

### RESPONDENTS' BRIEF

### OPINION BELOW

The opinion of the United States Circuit Court of Appeals for the Ninth Circuit is reported in 10 Fed. (2d) 915 (R. I, 131). No opinion was written by the district court.

## STATEMENT OF GROUNDS ON WHICH JURISDICTION OF THIS COURT IS INVOKED BY PETITIONER

“(a) The act of the Circuit Court of Appeals for the Ninth Circuit in holding that the bankrupt estate is liable for penalties accruing during the pendency of the bankruptcy is contrary to Section 57j of the Bankruptcy Act and defeats the purpose and scope of the Bankruptcy Act as defined by Congress.

“(b) That the act of the Circuit Court of Appeals for the Ninth Circuit is of peculiar public interest and presents a fundamental question of law upon which there should be no diversity of opinion in the several Circuit Courts of Appeal. That the decision of the Circuit Court of Appeals for the Ninth Circuit is in direct conflict with the Circuit Court of Appeals for the Seventh Circuit, in the case of *In re Messenger's Merchants Lunch Rooms, Inc.*, 85 Fed. (2d) 1002, and with the Circuit Court of Appeals for the Third Circuit in the case of *New Jersey v. Pressed Steel Car Co.*, 100 Fed. (2d) 147. That the uncertainty created by the conflict in the Circuit Courts adversely affects the expeditious administration and closing of innumerable pending bankruptcy cases and will continue to so affect such cases and future bankruptcy cases until and unless this Court shall exercise its power of supervision and hear and determine the present question.” (P. 7.)



## JUDGMENTS TO BE REVIEWED

On December 15, 1938, the court below entered a decree reviewing the order of the lower court in each of the two causes on appeal (R. I, 144; R. II, 57), one entitled Ray Ingels, Director of Motor Vehicles of the State of California, Howard E. Deems, as Registrar of Motor Vehicles of the State of California, and the Motor Vehicle Department of the State of California, appellants, vs. L. Boteler, trustee of the estate of Richmaid Creameries, Inc., a corporation, debtor, appellee, No. 8711; and the other entitled Ray Ingels, Director of Motor Vehicles of the State of California, and Howard E. Deems, as Registrar of Motor Vehicles of the State of California, appellants, vs. L. Boteler, Trustee of Richmaid Creameries, Inc., a corporation, appellee, No. 8761.

Said causes were consolidated in the court below for briefing, argument and decision (R. II, 57), and for convenience we have referred and shall hereinafter refer to the record in appeal No. 8711 as R. I, and in appeal No. 8761 as R. II.

### **SPECIFIC CLAIMS ADVANCED AND RULINGS MADE IN THE LOWER COURT WHICH ARE RELIED UPON BY PETITIONER AS THE BASIS OF THIS COURT'S JURISDICTION (p. 10)**

1. That the lower court erred in holding that section 57j of the Bankruptcy Act is not applicable to penalties which accrue during the course of the administration of a bankrupt estate, while the estate



is being operated incidental to its liquidation. (R. I, 140.)

2. That the lower court erred in holding that the State of California has a lien on the property of the bankrupt estate which lien accrued during the course of administration of the bankruptcy estate. (R. I, 141.)

3. That the lower court erred in holding that the act of June 18, 1934 (48 Stat. 993, 28 U. S. C. A. Sec. 124a) subjects the trustee in bankruptcy to liability for penalties attached to state taxes (R. I, 141); and

4. That the lower court erred in holding that both the district court and the referee in bankruptcy erred in finding that the trustee had no funds with which to pay the motor vehicle taxes. (R. I, 137.)

### **JURISDICTIONAL STATUTORY PROVISION**

The jurisdiction of this court is invoked by petitioner under section 240 of the Judicial Code, 28 U. S. C. A. 347. No reference is made by petitioner to cases believed to sustain jurisdiction. (P. 10.)

### **QUESTION PRESENTED BY PETITION**

The petition presents one question only, namely (p. 2):

“Is a bankrupt estate liable for penalties imposed by state statutes for nonpayment of automobile license fees where license fees and penalties claimed accrued during operation for

purposes of liquidation of the business of the bankrupt estate by the Trustee in Bankruptcy?"

### STATEMENT OF CASE

The facts as set forth in the petition, which petitioner states were taken from the opinion of the court below and upon which the foregoing question arose (p. 3), are not as fully stated as we think they should be, and, therefore, since the factual matters are brief and undisputed, we shall state them in full from the opinion (R. I, 131-137):

"The Richmaid Creameries, Inc., filed its petition under Section 77b of the Bankruptcy Act (11 U. S. C. A., Sec. 207) in the court below on September 16, 1936, and on the same day John H. Chamness was appointed temporary trustee, with authority to operate the business of the debtor. Prior to September 16, 1936, The Richmaid Creameries, Inc., was engaged in the creamery business in Wilmington, California, owning certain milk and ice cream routes and making deliveries thereon and operating twenty-seven automobiles and trucks in the course of such business.

"The temporary trustee began to operate the business and borrowed money for that purpose, but his first month of operation of the business resulted in a loss of \$2,865.00. On December 22, 1936, the District Court entered an order directing liquidation of the assets of the debtor, continuing the trustee in office for that purpose, and referred the estate generally to the referee for further administration.

“January 5, 1937, a schedule of assets and liabilities of Richmaid was filed, showing assets of \$148,380.02, and liabilities of \$87,089.64, including \$2,000.00 borrowed by the trustee on certificates.

“January 20, 1937, L. Boteler, appellee here, was appointed trustee in bankruptcy for the purpose of liquidating the assets of Richmaid.

“During the months of January and February, 1937, and up to and including February 27, 1937, the temporary trustee and the trustee, respectively, continued to operate the business of Richmaid and to make the usual deliveries of milk and ice cream on the aforesaid ‘routes.’ The trustee issued checks against the estate in payment of expenses in connection with the operation of the business. When there were insufficient funds in the estate to pay the checks, the trustee, on some occasions cashed the same out of his own personal funds and held the checks until there were sufficient funds in the bankrupt estate with which to pay the same.

“The total receipts of the trustee from September 16, 1936, to January 19, 1937, were \$70,006.23, and the total disbursements for the same period were \$79,647.65; the total receipts from January 20, 1937, the date when the appellee assumed trusteeship of the estate of Richmaid, to February 4, 1937, were \$7,899.61, while the total disbursements for the same period were \$7,624.46.

“Automobile license fees are due and payable in the state of California on the first day of January of each year, to be paid at the time of registration or renewal thereof. (Sec. 3, Calif.

Vehicle License Fee Act (Ch. 362, Cal. Stats. 1935, as amended). Delinquency arises upon operation of a vehicle upon any highway of the State without the license fee having been paid and a penalty attaches if the fee is not paid within 30 days. (Sec. 6, *ibid.*) The penalty is by law added to the fee upon any application for annual renewal of registration made on or after February 5, unless the vehicle has not been operated on the highways of the state since the expiration date. (Sec. 378 (b) Calif. Vehicle Code.) Section 379 (a) of the California Vehicle Code provides that every registration or transfer fee and any penalty added thereto from the time the same became due, constitute a lien upon the vehicle for which due.

“Continuously during the month of January, 1937, and to and including February 27, 1937, the temporary trustee and the trustee operated the Richmaid automobiles and trucks upon the public highways of the state of California, carrying on the business of Richmaid.

“The trustee did not pay the California 1937 license fees upon said vehicles, in the amount of \$410.90, prior to February 5, 1937. On February 28, 1937, the referee made an order confirming the sale of Richmaid's milk and ice cream delivery routes and certain equipment, for the sum of \$8260.00. This was the first property sold in liquidation, and the trustee did not thereafter attempt to operate the business of the debtor.

“On or about February 27, 1937, 23 days after the statutory delinquency date, the trustee made application to the Department of Motor Vehi-

cles of the State of California for 1937 licenses for the motor vehicles referred to, tendering the fees, but not the penalties demanded by the statutes of California for violation of its motor vehicle license laws. Because of the refusal of the trustee to pay the penalties required by the laws of the state of California, the 1937 licenses were not issued to him.

"Thereafter, the trustee filed a petition with the referee for an order requiring the appellants here to show cause why the penalties assessed against the Richmaid motor vehicles should not be set aside and, further, to show cause why the 1937 license plates for said motor vehicles should not be issued to the trustee upon payment of the fees, exclusive of the penalties. Following this, the trustee filed an amended petition to require the appellants to show cause why they should not be required immediately to file such claims as they assert against the bankrupt estate or be forever barred from asserting such claims against said estate or against the motor vehicles, and further requiring said appellants to show cause why the trustee should not be authorized to sell the motor vehicles free and clear from any and all liens claimed by the motor vehicle department of the state of California upon said vehicles.

"The referee made certain findings of fact, most of which are set forth above, but, in addition, the referee made findings as follows:

"The court further finds that the trustee herein had absolutely no funds in his possession between the date of his appointment on the 20th day of January, 1937 and the 27th

day of February, 1937 with which to purchase the 1937 license plates for said motor vehicles . . . .

‘The court further finds that at no time prior to the 27th day of February, 1937, did said trustee have funds with which to pay said registration and license fees owing upon said motor vehicles and that the same condition existed from the date that the order of liquidation was made herein, to-wit, the 22nd day of December, 1936 to the date of the appointment of L. Boteler, the present trustee on the 20th day of January, 1937. That during the month of January, 1937 and up to the said 27th day of February, 1937, the trustee herein and his predecessor operated said vehicles upon the public highways of the State of California without the payment of any registration and license fees for said year.’

“The referee made an order setting aside all penalties assessed against the motor vehicles and directed the trustee to sell said motor vehicles free and clear of any and all liens thereon arising by reason of the failure of the trustee to pay the motor vehicle license tax provided under the laws of the state of California and commanding Ingels and Deems to file claims in the bankruptcy proceeding for the registration and license fees upon said motor vehicles within 30 days from the date of the order or be forever barred from asserting any claim or claims for taxes and/or registration or license fees against said motor vehicles and against this bankrupt



estate or the trustee herein, either in his official capacity as such trustee or individually.' The appellants petitioned the District Court to review the said order and the District Judge denied the petition and confirmed the order of the referee.

"In addition, the trustee had petitioned the referee for an order directing the appellants to receive the principal of the license fees in full payment of any and all sums owing by Richmond on said motor vehicles and enjoining collection or attempted collection by them of any penalties which the statutes of the state of California compelled them to collect. The referee declined to include such mandate in his order, and the trustee made application to the District Court, for a mandatory injunction directed to the appellants, requiring them to receive the statutory fees less the penalties and to deliver the license plates to the trustee, which issued the order as prayed.

"An appeal was allowed Ingels, Director of Motor Vehicles of the State of California, and Deems, as Registrar of Motor Vehicles, from each order."

## ARGUMENT

### I

Section 57j of Bankruptcy Act is not applicable.

### II

Act of June 18, 1934, c. 585, 48 Stat. 993 (28 U. S. C. A. 124a) is applicable.



### III

Decision of court below not in conflict with the decision of another circuit court of appeals on the same matter.

### IV

Court below did not err in holding that the State of California has a lien on the motor vehicles for licensee fees and penalties which accrued during administration of the bankrupt estate.

### V

Court below did not err in holding that the trustee had funds with which to pay the motor vehicle license fees.

### I

#### **Section 57j of Bankruptcy Act Is Not Applicable**

Section 57j of the Bankruptcy Act (11 U. S. C. A. 93j) reads as follows:

“Debts owing to the United States, a State, a county, a district, or a municipality as a penalty or forfeiture shall not be allowed; except for the amount of the pecuniary loss sustained by the act, transactions, or proceeding out of which the penalty or forfeiture arose, with reasonable and actual costs occasioned thereby and such interest as may have accrued thereon according to law.”

Debt is defined in section 1, subd. (11), of the Bankruptcy Act as follows:

“‘Debt’ shall include any debt, demand, or claim provable in bankruptcy;”

The court below said in its decision that,

“Obviously, the section refers to debts owing by the bankrupt and not by the trustee.” (R. I. 140)

The court further said,

“If the taxes in question were due and payable at the time of the filing of the petition, they would be provable, and it follows, under Section 57 (j) of the Act (11 U. S. C. A. Sec. 93 (j)), penalties thereon would not be allowable, save to the extent permitted by said section. (R. I. 138.)

“But here we are confronted with a different set of facts. These taxes became fixed by reason of the operation of the business by the trustees, after the date of the filing of the petition and after the date of what in effect amounted to an adjudication. It should be obvious that a debt or claim created thereby was not provable, not being in existence at the time of the filing of the petition and, therefore, not dischargeable.” (R. I. 138.)

In *Cantor vs. Cherry* (C. C. A. 3), 73 Fed. (2d) 188, 189, the court said:

“In order to prove a claim in bankruptcy, the obligation must have been in existence at the time of the filing of the petition.” (Certiorari denied, 293 U. S. 626, 55 S. Ct. 346, 79 L. Ed. 712.)

Even a contingent liability of the bankrupt is not a debt provable in bankruptcy (*Colman Co. vs. Withoft* (CCA 9), 195 Fed. 250), much less is a lia-

bility created by a trustee of the bankrupt estate, such as we have in the instant case.

The decision of the court below correctly states the law in the following language:

“Whether a debt or claim is provable in bankruptcy turns upon its status at the time of the filing of the petition (Sec. 760, Remington on Bankruptcy, 4th ed.); claims not owing at the time of filing of the petition are not provable (Sec. 807, Remington; *Colman Co. v. Withoft* (CCA 9), 195 F. 250, 252; *Cantor v. Cherry* (CCA 3), 73 F. (2d) 188.) Section 1 (9) of the Bankruptcy Act (11 U. S. C. A., Sec. 1) includes, in the definition of ‘creditor’ anyone who owns a demand or claim provable in bankruptcy. While actually neither demand nor claim, taxes are ‘provable’ in their nature. (Sec. 845, Remington).” (R. I, 137.)

Therefore, section 57j of the Bankruptcy Act, which pertains to debts, demands and claims provable in bankruptcy, is not applicable to the question of the liability of the bankrupt estate for penalties imposed by state statutes for nonpayment of automobile license fees where license fees and penalties claimed accrued during and by reason of the operation of the business of the bankrupt estate by the trustee for the purpose of liquidating the assets of said estate for the benefit of creditors.

II. °

**Act of June 18, 1934, Is Applicable**

The act of June 18, 1934, Chapter 585, 48 Stats. 993 (28 U. S. C. A. 124a), reads as follows:

**“STATE TAXATION; BUSINESS CONDUCTED BY RECEIVERS, TRUSTEES, OR OTHER COURT OFFICERS SUBJECT TO**

Any receiver, liquidator, referee, trustee, or other officers or agents appointed by any United States court who is authorized by said court to conduct any business, or who does conduct any business, shall, from and after June 18, 1934, be subject to all State and local taxes applicable to such business the same as if such business were conducted by an individual or corporation: **PROVIDED, HOWEVER,** That nothing in this section contained shall be construed to prohibit or prejudice the collection of any such taxes which accrued prior to June 18, 1934, in the event that the United States court having final jurisdiction of the subject matter under existing law should adjudge and decide that the imposition of such taxes was a valid exercise of the taxing power by the State or States, or by the civil subdivisions of the State or States imposing the same.”

The court below in its decision said:

“By the Act of June 18, 1934, (48 Stat. 993, 28 U. S. C. A. Sec. 124 (a)), a trustee who is authorized by any United States Court to conduct any business, and does so, is subject to all State and local taxes applicable to such business the same as if such business were conducted

by an individual or corporation.' This is sufficient basis for the attachment of the penalty and lien." (R. I, 141.)

The court further said:

"The right of the trustee, under order of the court, to operate the business for a limited period cannot be challenged, but the estate, save as to existing lienholders not consenting—of which there are apparently none here, is liable for the charges incurred, even to the extent of the depletion of the assets of the estate, even to the detriment of labor claimants. The reason is simple: The operation of the business in such situation is for the benefit of the creditors. Remington, Sec. 2662, 445, 446. (R. I, 138.)

"The motor vehicle license or registration fee is a privilege tax levied in exercise of the police power to control and regulate travel on the public highways. It is not considered as a tax on the motor vehicle itself, but for the privilege of using the highways. *Blashfield, Cyc. of Automobile Law*, Sec. 212, Vol. 1, p. 158. A license to operate a motor vehicle is granted under the inherent right of the state or municipality to regulate its use on the public highways or streets. *Ibid.*, Sec. 211, p. 157. The only automobiles required to be registered under the California Motor Vehicle Act are vehicles to be used upon the public highway (*Cal. Stats. 1927*, p. 1424; *California Standard Finance Corp. v. Riverside Finance Co.*, 111 Cal. App. 151, 163, 295 P. 555); if the vehicles were not used, no registration fee would have fallen due under the law of California. But, in carrying on the business

of Richmond, the motor vehicles were operated upon the public highways of the state of California and thereby the registration and license fees attached. They were not paid, but became delinquent, and on February 5, 1937, the penalties prescribed by law applied. California Vehicle Code, Sec. 370, *et seq.*; California Vehicle License Fee Act, Sec. 6. (R. I, 139.) (Statutes and Code sections mentioned above are set forth in the Appendix hereto.)

"The motor vehicles in question could not be operated in 1937 without incurring the license and registration fees. Necessarily, therefore, the fees were an expense of doing business and were chargeable against the estate. The trustee has the duty of seeking out and paying all taxes (Sec. 847, Remington). He knew, or should have known, that a license fee was required before the motor vehicles could be legally operated upon the public highways, although, if the motor vehicles had not been used the fees would not have become payable.

"Were the motor vehicles operated by Richmond itself, or any other person or corporation, there would be no question of liability for the penalties. Is a trustee operating a business absolved from compliance with law?"

— "The normal course of procedure in bankruptcy is liquidation, not continuance of the business of the bankrupt. Where the business of the bankrupt is conducted for a limited period by the trustee, upon order of the court, the purpose is to benefit the creditors. The expenses of operation must be paid out of the estate.



That the license and registration fees are legitimate expenses, there can be no question." (R. I, 139-141.)

The court below, in holding that the estate is liable for the penalties, quoted the authorities as follows:

"The Supreme Court, in the case of *Swarts v. Hammer*, 194 U. S. 441, 444, said: 'By the transfer to the trustee no mysterious or peculiar ownership or qualities are given to the property. It is dedicated, it is true, to the payment of the creditors of the bankrupt, but there is nothing in that to withdraw it from the necessary protection by the State and municipality, or which should exempt it from its obligations to either.' (R. I, 141.)

"In *State of California v. Hisey*, 84 F. (2d) 802, 805, a receivership case, we held that the appointment of a receiver by a court of equity could not have any effect upon the right of the State of California to collect penalties for unpaid taxes; that receivers had been compelled in numerous cases to pay penalties for nonpayment of taxes which accrued subsequent to their appointment. We further held that if the penalty, as well as the tax, is a lien upon the property in the hands of a receiver, as the statutes of California provide, it is difficult to see how the payment of the penalty can be differentiated from the payment of the lien for the tax \* \* \*. The penalty is a part of the tax. \* \* \*. Compare *Michigan v. Michigan Trust Co.* 286 U. S. 334, 344; *People v. Hopkins* (CCA 2), 18 F. (2d) 731, 733; *McFarland v. Hurley*



(CCA 5), 286 F. 365, 366; *Coy v. Title Guarantee & Trust Co.* (CCA 9), 220 F. 90, 92.

"This view is upheld by the United States Circuit Court of Appeals for the Second Circuit. In the case of *In re Humeston*, 83 F. (2d) 187, 189, that court said:

\* \* \* Such taxes as fell due during the period of the trustee's occupation were part of the expenses of that occupation and should be borne by the estate. \* \* \* When \* \* \* the mortgagor's trustee continues the occupation, he necessarily means to exploit it for profit, and the gross returns must pay the running expenses. Thus taxes which became payable between November 1, 1933, and May 21, 1935, must be paid, and not only the entire face of these, but all interest and penalties accumulated upon them. It was the trustee's duty to pay them when they fell due and the estate must suffer from his failure. \* \* \* (Emphasis is by the court.) (R. I, 142.)

"Additional authority may be found *In re Preble Corporation* (D. C. Me.), 15 F. Supp. 775, 776 (Aff. on different grounds 84 F. (2d) 73; cert. den. 299 U. S. 575):

"Generally, speaking, property in the custody and control of federal receivers and trustees is subject to taxation under state law the same as any other property. \* \* \* (Cases cited.)

\* \* \*

"A proper performance of the duty to protect the property intrusted to its agents by the court requires the payment of taxes. In this case taxes

are a part of the necessary expense of carrying on the business.

“The trustee is subject to all state and local taxes which are applicable to the business which he conducts.”

“If the trustee fails to pay taxes in a proper case, although he has sufficient funds to do so, and thereby subjects the estate to interest and penalties, he will be surcharged to the extent of such interest and penalties.” Gerdes on Corporate Reorganizations, vol. 1, section 400.” (R. I, 143.)

In the case of *In re Humeston*, 83 Fed. (2d) 187, a bankruptcy matter, quoted by the court below in its decision, the trustee took possession of certain real-estate belonging to the bankrupt estate and collected the rents therefrom. He failed to pay the taxes that accrued while the property was in his possession and finding that there was no equity left in the property over and above encumbrances, desired to abandon it. This the referee refused to allow, and ordered the trustee to sell the property subject to all liens. The mortgagees filed a petition claiming the rents. This the referee refused to allow. Appeals were taken from these two orders. The court held:

“However, they (mortgagees) were entitled to some relief. Such taxes as fell due during the period of the trustee's occupation were part of the expenses of that occupation and should be borne by the estate (citing authorities). This is not contrary to our decision *In Re Kings*

*County Real Estate Corporation (C.C.A.)* 67 F. (2d) 895. There, a second mortgagee had got the rents sequestered in his favor, and we held that he might take them without deduction, leaving unpaid even those taxes which accrued during occupation. In this we followed the New York law, *Ranney vs. Peyser*, 83 N. Y. 1. The distinction is that a mortgagee who enters or gets a sequestration order does not by that alone embark upon a venture on the land; he is merely collecting his debt. He may indeed, as we suggested, put himself in the same class as the mortgagor, if for instance he delays foreclosure so long that it is reasonable to infer that he is using the land as an independent enterprise; but the sequestration is not enough without more. When on the other hand the mortgagor's trustee continues the occupation, he necessarily means to exploit it for profit, and the gross returns must pay the running expenses. Thus taxes which became payable between November 1, 1933, and May 21, 1935, must be paid, and not only the entire face of these, but all interest and penalties accumulated upon them. It was the trustee's duty to pay them when they fell due, and the estate must suffer from his failure. The first order will therefore be modified to conform to this disposition. (Order dismissing petition of mortgagees claiming the rents.)

"We cannot see by what warrant the mortgagees challenge the sale of the equity. It is true that they are general creditors as well as lienors, but as creditors they can have no interest in preventing a sale; and as mortgagees it cannot affect their remedies in any way whatever.

“Order denying the motion for payment of rents modified as above; appeal dismissed from the order directing sale.”

We are unable to perceive of any legal reason why the bankrupt estate herein should not suffer if the bankrupt estate *In re Humeston, supra*, had to suffer by the payment of penalties for the failure of the trustee to pay taxes when due on property from which he had collected rents during the administration of the estate. The trustee in the instant case used the highways of the State of California for the purpose of delivering milk and ice cream by motor vehicles in carrying on the business of the bankrupt estate. In so conducting this business it was his duty to pay the State's fees for such use of the highways, and it follows that from his failure to pay said fees when due, the bankrupt estate is liable for penalties.

The holding of the court below that the act of June 18, 1934 (28 U. S. C. A. 124a), is applicable and not section 57j of the Bankruptcy Act, is supported by the weight of authority. The decision does not defeat the purpose or scope of the Bankruptcy Act as defined by congress, as contended by petitioner, but places a legal duty on a trustee in bankruptcy to pay all taxes when due where he operates the business of the bankrupt, which are applicable to such business. This was the intention of congress when it passed the act of June 18, 1934. And the decree of the court below, in ordering the taxes and penalties paid on the motor vehi-

cles disposed of subject to the lien for taxes and penalties (R. I, 145), is in accord with the decree of the Circuit Court of Appeals for the Second Circuit in the case of *In re Humeston, supra*.

### III

#### Decision of Court Below Not in Conflict With Decision of Another Circuit Court of Appeals on the Same Subject

“In so far as the decision *In re Messenger's Merchants Lunch Rooms, Inc.* (CCA 7), 85 F. (2d) 1002, cited by the appellee as authority for affirmance, is in conflict herewith, it is expressly disapproved.” (R. I, 144.)

It is upon the authority of the above case and the case of *In re Pressed Steel Car Co. of New Jersey*, 100 Fed. (2d) 147, decided by the Circuit Court of Appeals for the Third Circuit, that petitioner seeks to invoke the jurisdiction of this court. (P. 7.)

In the case of *In re Messenger's Merchants Lunch Rooms, Inc.*, the State of Illinois filed a claim with the bankruptcy court seeking to recover penalties, under the Retailers' Occupational Tax Law of the state, on sums due prior to the filing of the petition in bankruptcy and on sums due by the receivers in the operation of the bankrupt's business. The district court disallowed the claim and its order was affirmed by the circuit court of appeals upon the grounds, first, that penalties are not provable in bankruptcy; second, that the Act of

June 18, 1934 (28 U. S. C. A. 124a), applies only to taxes and not to penalties; and, third, that the conditions precedent, necessary to the recovery of penalties provided in said law, were not complied with.

The second ground is the only one which requires attention of this Honorable Court in passing upon the petition herein, because as to the first ground, it is well settled that penalties as such are not provable in bankruptcy, and the facts in the instant case show that no attempt was made by respondents to have the bankruptcy court allow penalties; and as to the third ground, that situation is not present in the instant case.

As to the holding that the act of June 18, 1934, applies only to taxes and not to penalties (second ground), the court was not then considering, nor did it have before it, a statute which made the penalty a part of the tax. This feature of the California statute was considered by the court below in the instant case. The court said:

"Automobile license fees are due and payable in the state of California on the first day of January of each year, to be paid at the time of registration or renewal thereof. (Sec. 3, Calif. Vehicle License Fee Act (Ch. 362, Cal. Stats. 1935, as amended).) Delinquency arises upon operation of a vehicle upon any highway of the State without the license fee having been paid and a penalty attaches if the fee is not paid within 30 days. (Sec. 6, *ibid.*) The penalty is by law added to the fee upon any application for annual renewal of registration made on or



after February 5, unless the vehicle has not been operated on the highways of the state since the expiration date. (Sec. 378 (b) Calif. Vehicle Code.) Section 379 (a) of the California Vehicle Code provides that every registration or transfer fee and any penalty added thereto, from the time the same became due, constitute a lien upon the vehicle for which due." (R. I, 133.) (Statutes and code sections set forth in Appendix.)

\* \* \* \* \*

"In *State of California v. Hisey*, 84 F. (2d) 802, 805, a receivership case, we held that the appointment of a receiver by a court of equity could not have any effect upon the right of the State of California to collect penalties for unpaid taxes; that receivers had been compelled in numerous cases to pay penalties for nonpayment of taxes which accrued subsequent to their appointment. We further held that 'If the penalty, as well as the tax, is a lien upon the property in the hands of a receiver, as the statutes of California provide, it is difficult to see how the payment of the penalty can be differentiated from the payment of the lien for the tax.' \* \* \* The penalty is a part of the tax \* \* \* Compare *Michigan v. Michigan Trust Co.*, 286 U. S. 334, 344; *People v. Hopkins* (CCA 2), 18 F. (2d) 731, 733; *McFarland v. Hurley* (CCA 5), 286 F. 365, 366; *Coy v. Title Guarantee & Trust Co.* (CCA 9), 220 F. 90, 92." (R. I, 142.)

Therefore, as to the case of *In re Messenger's Merchants Lunch Rooms, Inc.*, *supra*, we think it



distinguishable in two important respects, first, that the Retailers' Occupational Tax Law of Illinois did not make the penalty a part of the tax and, second, that a claim for the allowance of penalties was there under consideration, whereas, the instant case involves merely the right of the State of California to refuse to register and issue license plates for motor vehicles of a bankrupt estate where the trustee refuses to pay penalties on delinquent taxes which accrued by reason of the operation of such motor vehicles on highways of the state by the trustee in carrying on the business of the estate.

In the mentioned case of *In re Pressed Steel Car Co.* of New Jersey, the state of New Jersey filed a claim seeking to recover corporation franchise taxes and a penalty of 1 per cent per month. The district court disallowed the claim for taxes as well as the penalty. The circuit court of appeals reversed the lower court and directed the lower court to allow the claim for taxes but not for the penalty and directed the lower court to proceed in conformity with the opinion of the circuit court, which opinion went no further than to say, in regard to the allowance of penalties (p. 153), that section 57j of the Bankruptcy Act prohibits the allowance of penalties upon claims in bankruptcy proceedings and that,

"In the case at bar we presume that the State of New Jersey will not object to receiving simple interest and if this be so, such interest should be allowed on the claims."

The above case is not an authority against which the decision in the instant case conflicts. There, a claim for the allowance of a penalty was filed. In the instant case respondents did not file a claim and in fact refused so to do and objected to the jurisdiction of the referee in bankruptcy to order them to file a claim, which objection was overruled. (R. I, 23.)

The decree of the court below did not direct the district court to allow a claim, but directed said court to order the regulation and license fees and accrued penalties paid, or, in the alternative, to permit the motor vehicles to be disposed of subject to the lien of the State of California for the unpaid taxes and penalties. (R. I, 144.) In other words, the lien of the State was recognized by the upper court.

For the foregoing reasons the decision herein is not in conflict with the decision in either of the above cases cited by petitioner.

#### IV

**The Court Below Did Not Err in Holding That the State of California Has a Lien on the Motor Vehicles for License Fees and Penalties Which Accrued During Administration of the Bankrupt Estate**

The decision of the court below states,

"Section 379 (a) of the California Vehicle Code provides that every registration or transfer fee and any penalty added thereto from the

time the same became due, constitutes a lien upon the vehicle for which due." (R. I, 133.)

Section 6 of the California Vehicle License Fee Act (See Appendix) provides as follows,

"Every license fee and any penalty added thereto, from the date the same becomes due, constitute a lien upon the vehicle for which due."

The court further stated in its decision,

"The general rule is that the law of the state will control as to the nature of a lien, its creation, the time of taking effect. See. 1891, Remington. Under Section 124 (a) of 28 U. S. C. A., it follows that the lien in this case is valid." (R. I, 141.)

Petitioner fails to point out how or in what manner the holding of the court below conflicts with the decision of another circuit court of appeals. He rests his specification of error on the contention that section 57j of the Bankruptcy Act is applicable and not the act of June 18, 1934. (P. 10.)

The Bankruptcy Act, as it read at the time of the present litigation, provides in section 67n (11 U. S. C. A. 107 (d)), that the validity of,

"Liens given or accepted in good faith and not in contemplation of or in fraud upon the provisions of this title, and for a present consideration, which have been recorded according to law, if record thereof was necessary in order to impart notice, shall, to the extent of such present consideration only, not be affected by anything herein."

The present consideration for the lien in the instant case is unpaid taxes and penalties; the latter by the laws of the State of California became a part of the taxes.

We have heretofore shown that section 57j is not applicable in the instant case. Therefore the court below did not err in holding that the State of California has a lien on the motor vehicles for license fees and penalties which accrued during administration of the estate.

**V**

**The Court Below Did Not Err in Holding That the Trustee Had Funds With Which to Pay the Motor Vehicle License Fees**

Petitioner does not argue this specification of error. (P. 11.)

The court below in its decision, as to this matter, said:

“The referee made two findings of fact, set forth above, to the effect that the trustee had no funds with which to pay the license and registration fees prior to February 5, 1937. These findings are contrary to the true facts. Actually during the period January 20, 1937, to February 4, 1937, large sums of money were received by the trustee, all of which were received and paid out before the license became subject to penalty, without taking into account the moneys received and disbursed in the operation of the business from January 1, to January 19, 1937.” (R. I, 137.)

However, the point is immaterial whether the trustee was with or without funds sufficient to pay the taxes when they fell due. This matter is inconsequential and petitioner so treats it.

### CONCLUSION

The grounds upon which petitioner seeks to invoke the jurisdiction of this honorable court are untenable, because,

(a) The act of the Circuit Court of Appeals for the Ninth Circuit in holding that the bankrupt estate is liable for penalties accruing during the pendency of the bankruptcy is not contrary to section 57j of the Bankruptcy Act and does not defeat the purpose or scope of the Bankruptcy Act as defined by congress; and

(b) The decision of the Circuit Court of Appeals for the Ninth Circuit is not of peculiar public interest, nor is it in conflict with the decision of the Circuit Court of Appeals for the Seventh Circuit in the case of *In re Messenger's Merchants Lunch Rooms, Inc.*, *supra*, or with the decision of the Circuit Court of Appeals for the Third Circuit, in the case of *In re Pressed Steel Car Co. of New Jersey*, *supra*. The facts and state statutes considered by the court in those cases are not the same as were considered by the court below in the instant case.

For the reasons set forth herein by respondents, they respectfully submit that petitioner has failed

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to state grounds sufficient to invoke the jurisdiction  
of this honorable court.

Dated: April 5, 1939.

EARL WARREN,

Attorney General of  
the State of California.

By FRANK W. RICHARDS,

Deputy Attorney General of  
the State of California,

*Counsel for Respondents.*



## APPENDIX

Chapter 362, Statutes of 1935, Pages 1312-1315.

*"An act relating to licensing and taxing of vehicles, providing for license fees for the privilege of operating certain vehicles, providing for the exemption of such vehicles from all taxes according to value for State, county or municipal purposes, providing for the administration and enforcement of this act, creating a fund to be known as the motor vehicle license fee fund, and making an appropriation of the moneys therein.*

*"(Approved by the Governor June 25, 1935. In effect September 15, 1935.)*

*"The people of the State of California do enact as follows:*

*"SECTION 1. 'Vehicle' as used herein means every vehicle subject to registration under the Vehicle Code.*

*"'Department' means the Department of Motor Vehicles.*

*"SEC. 2. A license fee is hereby imposed for the privilege of operating in this State any vehicle. The annual amount of such license fee shall be a sum equal to one and three-quarters per cent of the actual market value of such vehicle, as determined by the department. The department annually shall compile and publish a list showing the market values as determined by it of each class of vehicle subject to the license fee hereby imposed, such vehicles being classified by make, type and year of manufacture. The license fee imposed by this act shall not apply to any vehicle not subject to registration under the Vehicle Code, nor to any vehicle*

owned by the State, any political subdivision of the State, or any city, city and county, county, district or public corporation.

“SEC. 3. Except as hereinafter provided, the license fee hereby imposed shall be due and payable to the department on the first day of January of each year. Such fee shall be paid to the department at the time of registration of such vehicle.

“SEC. 4. Upon vehicles registered for the first time in this State after the end of January of any year, the fee imposed by this act for such year shall be reduced one-twelfth for each month which shall have elapsed since the beginning of such year. No additional license fee shall be imposed under this act upon any vehicle upon the transfer of ownership of such vehicle if such license fee on such vehicle has already been paid for the year in which transfer of ownership occurs.

“SEC. 5. The license fee imposed under this act is in addition to any and all licenses and taxes otherwise imposed, except that no tax according to value shall hereafter be levied or imposed upon any vehicle upon which is paid the license fee required by this act. Such vehicles are hereby exempted from all taxes, State, county or municipal, according to value levied for State or local purposes.

“SEC. 6. Whenever any vehicle is operated upon any highway of this State without the license fee having first been paid as required by this act, such fee is delinquent. If such fee is not paid within thirty days after the same becomes delinquent, a penalty equal to such fee shall be added thereto and be collected therewith.

"Every license fee and any penalty added thereto, from the date the same becomes due, constitute a lien upon the vehicle for which due.

"The department shall collect such fee and any penalty by seizure of such vehicle from the person or persons in possession thereof, if any, and by the sale of such vehicle. The seizure and sale herein authorized shall be conducted and carried out by the department in the same manner as is provided by law for the seizure and sale of personal property by county assessors for the collection of taxes due on personal property. In the event, however, that the records of the department indicate that the registered owner of a vehicle so seized is not the legal owner thereof, as those terms are defined by the Vehicle Code, the department shall, before selling such vehicle, give notice to the legal owner of such vehicle by registered mail addressed to the last known address of such legal owner as shown by the records of the department, at least ten days prior to such proposed sale.

"SEC. 7. The duty of collecting the license fee imposed by this act and enforcing the provisions hereof is hereby imposed upon the department. The department shall give to each person paying such license fee a receipt therefor which shall sufficiently designate and identify the vehicle upon which such fee is paid.

"SEC. 8. The director of the department shall appoint and fix the salaries of such employees as may be necessary to administer and enforce the provisions of this act.

"SEC. 9. All moneys collected by the Department of Motor Vehicles under the terms of this act shall be reported daily to the State Controller

and at the same time deposited in the State treasury to the credit of the motor vehicle license fee fund, which fund is hereby created. The moneys in said fund are hereby appropriated as follows:

“(a) One per cent, or so much thereof as may be necessary for the use of the Department of Motor Vehicles in the enforcement of the provisions of this act.

“(b) Of the remainder of the moneys paid into said fund during the eighty-seventh and eighty-eighth fiscal years, twenty-five per cent thereof shall be paid quarterly to the cities and cities and counties of this State in the proportion that the total population of each such city or city and county bears to the total population of all cities and cities and counties in this State, as certified by the department. For the purpose of this subsection, the population of each city or city and county is that determined by the last Federal census. In the case of a city incorporated subsequent to the last census, or in the case of an unincorporated territory being annexed to a city subsequent to the last census, the department shall ascertain the population of the city or the annexed territory by multiplying the number of registered electors therein by three. The moneys so paid shall be expended by the cities and cities and counties for law enforcement and the regulation and control and fire protection of highway traffic.

“(c) Twelve and one-half per cent of said remainder of such moneys shall be paid quarterly during the eighty-seventh and eighty-eighth fiscal years to the counties and cities and counties of the State in the proportion that the population of each such county or city and county bears to the total

population of all the counties and cities and counties of the State, as certified by the department. For the purpose of this subsection, the population of each county or city and county is that determined by the last Federal census.

“(d) The balance of the moneys in said fund shall on order of the Controller be transferred to the general fund of the State. Out of such moneys so transferred there shall be set apart sufficient moneys in the amount of the principal and interest paid or necessarily to be paid during the eighty-seventh and eighty-eighth fiscal years on the bonds of the State issued under:

“(a) The ‘State Highways Act’, approved by the Governor March 22, 1909, and by a majority of the electors at the general election held November 8, 1910;

“(b) The ‘State Highways Act of 1915’, approved by the Governor May 20, 1915, and by a majority of the electors at the general election held November 7, 1916;

“(c) Section 2 of Article XVI of the Constitution as approved by a majority of the electors at a special election held July 1, 1919; and

“(d) Section 3 of Article XVI of the Constitution, as approved by a majority of the electors at the general election held November 2, 1920.

“SEC. 9. The license fee provided for by this act shall not be imposed on and after December 31, 1937; provided, however, that the terms of this act shall continue in full force and effect with respect to all license fees due thereunder and penalties on account of operations of vehicles subject thereto, to the end that the State may take



any and all steps necessary to collect the amount of such license fees and penalties.

"SEC. 9. If any section, subsection, clause, sentence or phrase of this act is for any reason held to be unconstitutional, such decision shall not affect the remaining portions of this act. The Legislature hereby declares that it would have passed the remaining portions of this act irrespective of the fact that any such section, subsection, clause, sentence or phrase of this act be declared unconstitutional."

California Vehicle Code, Statutes of 1935, Chapter  
27, Secs. 370, 376, 377, 378 and 379,  
Pages 147, 150 and 151.

"370. Registration Fees. A registration fee of three dollars shall be paid to the department for the registration of every vehicle of a type subject to registration, except for such thereof as are expressly exempted under this code from the payment of registration fees.

"376. When Registration Fees Payable. All registration fees and all fees required of a manufacturer, transporter, or dealer for any special plate or set of plates shall be paid at the time application is made to the department for such registration or such plate or plates. (Amended by Ch. 671, Stats. 1935.)

"377. Fees for Transfer of Registration. Upon application for the transfer of the title or any interest of an owner or legal owner in or to a vehicle registered hereunder, other than upon a transfer to a chattel mortgagee and other than



upon a transfer to a transferee not required hereunder to obtain the issuance to him of a new certificate of ownership and registration card, there shall be paid the following fees:

- “(1) For a transfer by the owner ----- \$1.00
- “(2) For a transfer by the legal owner. \$1.00
- “(3) For a transfer by the owner and legal owner at the same time----- \$1.00”

“378. When Fees Delinquent. Penalties.

“(a) Whenever any vehicle is operated upon any highway of this State without the registration fee having first been paid as required by this code, such fee is delinquent.

“(b) A penalty shall be added upon any application for annual renewal of registration made on or after February 5 unless the vehicle has not been operated on the highways since the expiration date.

“(c) If any other fee is not paid within thirty days after the same becomes delinquent a penalty shall be added thereto.

“(d) In every event the penalty shall be equal to the fee and shall be collected therewith. (Amended by Ch. 671, Stats. 1935.)”

“379. Seizure and Sale of Vehicle.

“(a) Every registration or transfer fee and any penalty added thereto, from the date the same became due, constitute a lien upon the vehicle for which due.

“(b) The department shall collect such fee and any penalty by seizure of such vehicle from the person or persons in possession thereof, if any, and by the sale of such vehicle. The seizure and sale herein authorized shall be conducted and carried

out by the department in the same manner as provided by law for the seizure and sale of personal property by the assessor for the collection of taxes due on personal property."

